

VZCZCXRO6200
RR RUEHCN RUEHGH
DE RUEHGZ #0283/01 1250854
ZNR UUUUU ZZH
R 050854Z MAY 09
FM AMCONSUL GUANGZHOU
TO RUEHC/SECSTATE WASHDC 0557
INFO RUEHGZ/CHINA POSTS COLLECTIVE 0164
RUEHBJ/AMEMBASSY BEIJING 0420
RUEHCN/AMCONSUL CHENGDU 0103
RUEHHK/AMCONSUL HONG KONG 0144
RUEHGH/AMCONSUL SHANGHAI 0106
RUEHSH/AMCONSUL SHENYANG 0110
RUEHIN/AIT TAIPEI 0119
RUCPDO/DEPT OF COMMERCE WASHDC
RUEATRS/DEPT OF TREASURY WASHDC 0084
RUEAIIA/CIA WASHDC 0149
RUEKJCS/DIA WASHDC 0145

UNCLAS SECTION 01 OF 02 GUANGZHOU 000283

SENSITIVE
SIPDIS

STATE FOR EAP/CM, S/P, INR/EAP
STATE PASS USTR CHINA OFFICE

E.O. 12958: N/A

TAGS: [ECON](#) [SOCI](#) [CH](#)

SUBJECT: CHINESE INTERNET PORTALS SPINNING A LARGER WEB

(U) This document is sensitive but unclassified. Please protect accordingly. Not for release outside U.S. government channels. Not for Internet publication.

11. (U) SUMMARY: China's online community is not simply a group of young men hanging out at home, at a university center or (less frequently today) in an internet cafe, whiling away the time, playing games, viewing the equivalent of Youtube (or Youtube itself when it's not blocked) and even occasionally searching for informational purposes. It has expanded, two of the nation's most successful Internet portals tell us, to include women and older users. Even during this economic downturn, the market for online programs and services has grown as new users log on for the first time. To meet their demands, Chinese companies have begun to develop original games and other applications for the first time in their history. Chinese Internet portals have adopted different business models, but the key question in this maturing market is whether will can differentiate themselves one from the other or whether their growing similarity will essentially offer users little real choice in services. END SUMMARY.

Reaching More Women ...

12. (SBU) Tencent and Netease, two of China's largest Internet companies, have traditionally targeted young men as their primary audience, but this is gradually changing. While males between ages 18 and 25 still represent a majority of users, Internet use has been rising among other segments of the population. Over the last 2 years Netease has seen 20% growth among female users, who now make up 43% of the total, according to Netease PR Specialist Grace Liu. As more women go online, Netease and its competitors are working on developing new games and applications that are aimed specifically at a female audience. Netease, which is traded on the NASDAQ stock exchange, is one of the largest online gaming companies in China and also operates the popular Internet portal 163.com. Founded in Guangzhou in 1997, Netease now has offices throughout China and has become the country's most profitable Internet company. Company executives told us their headquarters remains in Guangzhou.

More Middle-Aged Users,...

13. (SBU) Liu also told us that 20% of Netease's customers are over 38, and Tencent Administration Director Pauline Song says that middle-aged Internet users are increasing quicker than the company's traditionally young target audience. Tencent, which is headquartered in Shenzhen, operates China's most popular Internet portal site and the popular 'QQ' instant messaging software.

Tencent and Netease are both planning to expand their audience among adult users, but using very different strategies. This year Netease will introduce a new marketing campaign to attract more mature users. Tencent, on the other hand, still relies primarily on a younger audience. They plan to introduce new products which will appeal to their current users as they age. Recently, they introduced money management software for young adults who have just entered the workforce. In this way, Tencent hopes to broaden its customer base, maintaining younger audiences while aging along with current users.

And More Rural and Home Users

¶4. (SBU) Netease has also experienced a 50 percent increase in Internet use outside of major cities. Tencent's CEO Ma Huateng attributed this change largely to the Chinese government's efforts to expand Internet access in rural regions. This initiative will be expanded in the future, and the Internet portals' pool of new users will continue to grow.

¶5. (SBU) Users in smaller cities and rural regions are more likely than their urban counterparts to use Internet cafes, but the importance of Internet cafes in China has subsided in recent years. According to Ms. Liu, home Internet use has become so accessible in most areas that it now accounts for 70% of total Internet users, with only 10% logging on from Internet cafes. The rise in home Internet use has also increased the number of children getting online, as those under 18 are not allowed into Internet cafes.

Full Speed Ahead, Despite the Downturn

¶6. (SBU) South China's Internet portals are still growing rapidly

GUANGZHOU 00000283 002 OF 002

despite the economic downturn that is affecting so many other industries. Pauline Song of Tencent says that online gaming has grown faster during the downturn than before. Both Tencent and Netease have moved ahead with ambitious expansion plans. Tencent plans to open its new 39-storey headquarters in Shenzhen this year; the new building will be fully occupied almost immediately. This year, Tencent will also open a game development office in Boston, Massachusetts. Netease is moving forward with plans to build a new R&D center that, the company tells us, will more than double its current workforce; Grace Liu emphasized that the firm's plans have not been affected by the downturn at all. With growth in Internet use remaining so robust, both companies are confident in the future.

An Eastward Journey; Video Game Development Comes to China

¶7. (SBU) In 2001, executives from Netease traveled to Japan to meet with executives from Sony with the goal of acquiring the rights to release Sony gaming software within China. According to Liu, they were turned down. After the refusal, Netease opened its own design department and began to develop original games and software, making them one of the first Chinese companies to do so. Tencent and others have followed suit and are now developing original applications rather than simply translating and repackaging imported ones. In June 2008, Netease released the online role-playing game "A Westward Journey," the first game they had developed entirely in-house. The game, which incorporates elements of Chinese history into the storyline, currently has 220 million registered users. According to Tencent's Pauline Song, Internet gaming in China was a nearly USD 300 billion industry in 2008 and will grow even larger this year. Foreign gaming companies are no longer ignoring the Chinese market. Blizzard, an American software company, has signed a deal with Netease to introduce some Blizzard games, including the popular "World of Warcraft," in China this year. While they will continue to import foreign games, with the success of "A Westward Journey" both Netease and Tencent are focused increasingly on producing original software for the Chinese market.

Similar Goals, Competing Models

¶8. (SBU) While Tencent and Netease compete to attract the same users, they have adopted very different business models for generating revenue. Over the 12 years since they were founded, both

Netease and Tencent have gone from upstart companies with a few dozen staff members to international giants with thousands of employees and users numbering well into the hundreds of millions. Tencent, whose success was built on its "QQ" instant messaging software, has followed a model similar to that of Yahoo in the U.S. The company offers a wide variety of services, ranging from email to music sharing for little or no cost, and relies largely on advertising for revenue. Netease, on the other hand, offers some basic free email services, but charges for most of its content. The company's largest source of revenue by far is subscriptions to online games, which accounts for over 80% of the total. The two companies may be becoming more similar, however. In 2007 Netease introduced a free search engine and blogs to its website while Tencent has recently begun developing subscription-based online games similar to those Netease has already released.

GOLDBERG